

# TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: GENERAL EXCISE, Deny Representative Treatment to Marketplace Sellers

BILL NUMBER: HB 1655

INTRODUCED BY: LUKE

EXECUTIVE SUMMARY: States that a person who sells or assists in the sale of tangible personal property, provides customer service, processes payments, and controls the fulfillment process is a “seller” rather than a “representative,” and therefore has primary liability for the GET. We advise caution because some of the terms in this definition are not tightly defined, are not internally consistent, and could have ramifications beyond the intended targets.

SYNOPSIS: Amends the definition of “person” in section 237-1, HRS, such that the last sentence is changed to, “Any person who sells or assists in the sale of tangible personal property on behalf of another seller by providing customer service, processing payments, and controlling the fulfillment process shall be deemed the seller of the property, when sold, and the seller on whose behalf the sale is made shall be deemed to have made a sale at wholesale pursuant to section 237-4.”

Amends the definition of “representative” in section 237-1, HRS, to exclude a “person who sells or assists in the sale of tangible personal property on behalf of another seller and who provides customer service, processes payments, and controls the fulfillment process.”

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: This bill appears to be an effort to target “marketplace sellers,” namely those sellers who provide a framework for smaller sellers, most of whom are likely out of state, to sell into Hawaii (among other places). We understand that the marketplace sellers are presently taking the position that even if the marketplace seller has nexus with and must pay tax to Hawaii, it has no responsibility to collect and remit taxes when it is merely representing another seller that otherwise has no nexus with Hawaii.

The United States Constitution has been interpreted as providing two limits on the states’ powers to tax. These limits come from at least two places: first, the Due Process Clause, requiring a person to have “minimum contacts” with a state before that state is allowed to exercise police powers, including the power to tax, against that person; and second, the Commerce Clause, where the Supreme Court held in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), that if the Congress does not otherwise define the threshold for taxability, state tax may not be imposed upon a person unless there is “substantial nexus” with that person. Substantial nexus is more than minimum contacts, and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), appears to stand for the proposition that some physical presence is needed to establish substantial nexus.

In Hawaii, section 237-22(a) HRS, states that there shall be excepted or deducted from the values, gross proceeds of sales, or gross income so much thereof as, under the Constitution and laws of the United States, the state is prohibited from taxing, but only so long as and only to the extent that the state is so prohibited. *In re Grayco Land Escrow, Ltd.*, 57 Haw. 436, 559 P.2d 264, *cert. denied*, 433 U.S. 910 (1977), established that Hawaii already extends its general excise and use taxes to reach the limit of the Constitution (“Thus, in plain and unmistakable language, the statute evidences the intention of the legislature to tax every form of business, subject to the taxing jurisdiction, not specifically exempted from its provisions.”).

For marketplace sales, *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960), and *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 483 U.S. 232 (1987), hold that substantial nexus can be established through an independently contracted sales agent who acts in a state on behalf of another. Thus, whether or not “economic nexus” is ultimately found to be constitutional, nexus can and should be attributed from a marketplace provider under current law.

Obviously, it is easier from a revenue administration perspective to shift the responsibility for collecting and remitting tax to a marketplace provider with nexus in the State, as opposed to trying to chase down a myriad of small and large sellers scattered throughout the nation, and that is what this bill is trying to accomplish.

Technically, the bill could be tightened up.

- The bill is now internally inconsistent because the definition of a marketplace provider in the definition of “seller” is slightly different from the definition of a provider that is excluded from the definition of “representative.” They should be made consistent.
- “Providing customer service, processing payments, and controlling the fulfillment process” strike us as vague terminology. The Committee should consider tightening up the terms or allowing the Department of Taxation regulatory authority to do so.

Digested 3/1/2018



**TECHNET**  
THE VOICE OF THE  
INNOVATION ECONOMY



March 13, 2018



Honorable Donovan M. Dela Cruz, Chair  
Senate Ways and Means Committee

Hawaii State Capitol  
415 S Beretania St  
Honolulu, HI 96813

**RE: Opposition to HB 1655 – taxes on tangible personal property**

Dear Chair Cruz and members of the committee:

We ask that you do not pass HB 1655, a bill imposing new taxes on tangible personal property. Please avoid making the same mistakes South Dakota did.

HB 1655 will be seen by Hawaii consumers as a new tax and could erode your ability to protect Hawaii businesses from out-of-state tax collectors.

*First, consider problems created by the bills anticipated legal challenges:*

- Will not go into effect for several years, if ever
- Will cost Hawaii taxpayers in attorney’s fees and court costs
- May be rendered irrelevant by other state lawsuits or Congressional action

*Second, if the bill survives court challenges, they would:*

- Reduce the ability of Hawaii to protect its businesses from burdens imposed by other states
- Rely on new revenue extracted from Hawaii residents – not from out-of-state businesses
- Would generate only minimal new tax revenue
- Establish a new tax regime that is anything but equal, consistent, or fair

**Likely seen as a new tax by your constituents**

Hawaii residents will likely see this as a new tax since any tax collected will come from the pockets of Hawaii citizens, not from out-of-state businesses.

NetChoice polled Tennessee residents on a similar tax in that state. ([www.NetChoice.org/TNTaxPoll](http://www.NetChoice.org/TNTaxPoll)), and 56% said requiring them to pay tax on online purchases from out-of-state businesses would be a statewide tax increase so it is likely that similar results would occur if Hawaii citizens were polled.

**HB 1655 is likely to bring burdens on Hawaii businesses from other states**

Just by proposing this bill, Hawaii creates a dangerous precedent for other state revenue departments to follow. While this bill would apply only to remote sellers, it encourages other states to create similar laws that would impact Hawaii sellers.

## **No revenue would be generated from HB 1655 for several years, if ever. And the bill fritters away tax dollars on an unnecessary lawsuit**

HB 1655 will generate no revenue for the state unless and until the US Supreme Court overturns a century of established federal doctrine.

Following enactment this bill, groups like NetChoice and ACMA intend to seek an injunction and challenge the law. Immediate injunction of HB 1655 is likely, since even the state of South Dakota<sup>1</sup> stipulated that its similar “Kill Quill” law was unconstitutional.

On March 6, 2017, the State Circuit Court in South Dakota granted a motion for Summary Judgment against the state’s 2016 law, finding:

“Because each of the Defendants lacks a physical presence in South Dakota... the State acknowledges that under *Quill Corp. v. North Dakota*, the State of South Dakota is prohibited from imposing sales tax collection and remittance obligations on the Defendants.”

“The State further admits that this Court is required to grant summary judgment in Defendants’ favor, because of the *Quill* ruling.”

“This Court is duty bound to follow applicable precedent of the United States Supreme Court.”

“This is true even when changing times and events clearly suggest a different outcome; it is simply not the role of a state circuit court to disregard a ruling from the United States Supreme Court.”

If a similar injunction is obtained in Hawaii, the state could not enforce HB 1655.

It is likely that the US Supreme Court will have already decided on the *Quill* question even before this new tax law would make their way through the courts. As noted above, courts already enjoined and are now reviewing the legality of a similar law in South Dakota<sup>2</sup> and Indiana<sup>3</sup> and regulation in Alabama.<sup>4</sup> HB 1655 acts as a pile-on with no material benefit to Hawaii -- while incurring litigation costs for the state.

## **Passage of HB 1655 would erode state sovereignty**

Advocates for this bill claim that the purpose is to overturn the current *Quill* standard<sup>5</sup> of physical presence. Today, the *Quill* standard stops tax collectors in California, New York, or Illinois from harassing Hawaii businesses that have no physical presence in those states.

But passage of this bill would remove the protections of *Quill* and reduce the ability of Hawaii to protect its businesses from tax collectors across the country, forcing Hawaii businesses to travel across the country to defend themselves in foreign state courts.

State tax collectors would be the true “winners” if HB 1655 succeed in overturning the *Quill* standard. Hawaii citizens and Hawaii businesses would be the losers.

## **No new money would come into Hawaii**

Even if HB 1655 survives a Supreme Court challenge, *no new money would flow into Hawaii*. Any sales taxes collected as the result of these bills would come from the pockets of Hawaii residents -- not from out-of- state businesses.

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<sup>1</sup> See *South Dakota v. Wayfair Inc. et al*, Case No. 3:2016cv03019 (S.D. Dist. Ct. May 15, 2016).

<sup>2</sup> See Sandra Guy, *South Dakota sues four big online retailers over sales taxes*, Internet Retailer (April 29, 2016).

<sup>3</sup> Ind. Code § 34-14-1-1

<sup>4</sup> See Chris Morran, *Newegg Challenges Alabama Over Collection Of Online Sales Tax*, Consumerist (June 14, 2016)

<sup>5</sup> *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992) further confirmed the physical presence standard for sales tax collection. It protected Quill, a Delaware corporation with offices and warehouses in Illinois, California, and Georgia, from North Dakota tax collectors and North Dakota tax rules – a state where Quill had no physical presence.

## **Minimal tax revenue would be generated from HB 1655**

Today, most of the top e-retailers already collect for Hawaii. That includes Amazon, who accounted for 41% of online sales in Q1 2016.<sup>6</sup>

Some advocates cite a 2009 University of Tennessee<sup>7</sup> study to suggest a large windfall of uncollected sales taxes. However, the UT study is far out-of-date and fails to account for existing tax collection by Amazon and several other large e-retailers.

Even the US General Accounting Office predict collections are, at best, less than half of what the outdated University of Tennessee study promises.

The question, assuming HB 1655 survives in court, is whether the minimal tax revenue extracted from Hawaii citizens is enough to justify the legal costs, executive branch overreach, and erosion of state sovereignty?

## **HB 1655 creates a new tax that is not equal, consistent, or fair**

Tax advocates justify these bills by saying they “create a level playing field for all sellers.” However, HB 1655 foists disproportionate collection burdens on catalog and online retailers. When a customer enters a gift shop in Annapolis, the store does not ask for that customer’s home address to look up the tax rate and later remit the tax to the customer’s home state.

But HB 1655 would impose the burden of look-up, tax filing, and audit – on marketplace sellers. We fail to see how that would be equal, consistent, or fair so we ask that you reject HB 1655 to protect Hawaii businesses from out-of-state tax auditors, shield Hawaii citizens from a new tax and avoid costly litigation the state is likely to lose.

Thank you for considering our views and please let us know if we can provide further information.

Sincerely,

CompTIA

NetChoice

Internet Coalition

TechNet

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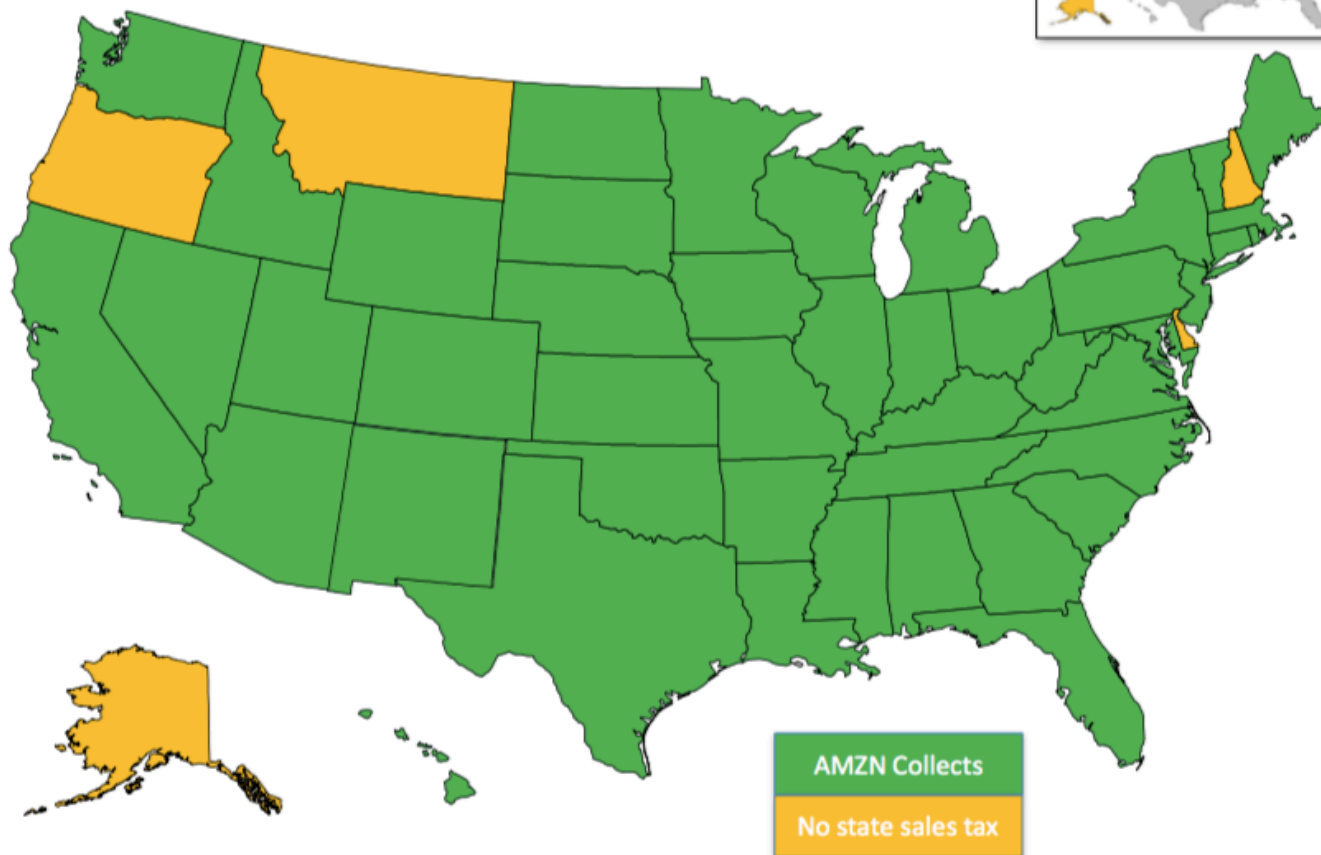
<sup>6</sup> Ken Kam, *The Market Is Underestimating Amazon*, Forbes (May 27, 2016).

<sup>7</sup> Bruce, Fox, and Luna, *State and Local Government Sales Tax Revenue Losses from Electronic Commerce*, University of Tennessee (2009).

NetChoice is a trade association of e-Commerce and online businesses. [www.netchoice.org](http://www.netchoice.org)

## Amazon is collecting for the entire country

Now 100% of the US population





To: The Honorable Donovan M. Dela Cruz, Chair  
and Members of the Senate Committee on Ways and Means

Date: Tuesday, March 13, 2018  
Time: 10:00 A.M.  
Place: Conference Room 211, State Capitol

**LATE**

From: Braden Cox, Director, US State & Local Public Policy  
Amazon  
**Written Testimony Only**

Re: HB 1655, Relating to Tax on Sales of Tangible Personal Property

Chair Dela Cruz and Members of the Committee:

We write regarding HB 1655, which would impose the state's general excise tax ("GET") on marketplaces that provide certain services to sellers. We oppose this legislation, at least as it is currently written, and offer the following on potential alternatives that would create a more level playing field and increase revenue compliance.

Many of you know Amazon as the online retailer we've become since first opening our virtual doors in 1995. You may not know, however, that there are more than 7,000 authors, sellers, and developers in Hawaii growing their businesses and reaching new customers on Amazon products and services.

We care about how small sellers can use our marketplace to reach customers nationwide. That's why we're concerned about HB 1655, which targets marketplaces that enhance the seller experience with customer service, payment processing, and order fulfillment services. As drafted, HB 1655 applies only to online marketplaces that offer these services, and would not uniformly apply to all the various online marketplace business models.

If fairness and increasing revenue collection are goals of this legislation, then there are better legislative options, including other pending legislation in Hawaii.

**Transferring the GET liability to marketplaces does not level the playing field, discriminates against and unfairly burdens certain marketplaces, and will not be a large revenue source for the state.**

HB 1655 applies to a very narrow type of business – marketplaces that provide customer service, process payments, and control the fulfillment process – thus it will not serve to level the playing field.

Many remote sellers do not make sales through a marketplace that provides these services. Additionally, it will be easy to avoid the obligations that HB 1655 creates. Those remote sellers that make sales through a marketplace can simply change their selling habits to avoid having GET remitted on their sales. Sellers will shift their sales to other sales channels that are not impacted by HB 1655. As

a result of HB 1655's very narrow application, HB 1655 will not serve to level the playing field between brick-and-mortar stores and remote sellers.

Furthermore, HB 1655 discriminates against and unfairly burdens marketplaces that provide customer service, process payments, and control the fulfillment process. These activities provide no reasonable basis on which to differentiate between marketplaces for purposes of applying the GET. All marketplaces regardless of the services they provide should be treated similarly for purposes of applying the GET.

Because of the very narrow application of HB 1655 and the ability of sellers and marketplaces to change their behavior to eliminate the bill's impact on them, the bill will not serve to raise any revenue for the state of Hawaii. To the extent the state is attempting to raise revenue by collecting GET on some portion of remote sales made into Hawaii, the state does not need to take action to do so because the U.S. Supreme Court is set to review the physical presence standard in *Quill Corp v. North Dakota*,

**HB 1655 is premature and unnecessary given that the U.S. Supreme Court will review the physical presences standard set forth in *Quill Corp v. North Dakota* this year.**

Hawaii does not need to take any legislative action to address the remote seller issue because the U.S. Supreme Court will be reviewing the validity of the physical presence standard set forth in *Quill Corp v. North Dakota*. The U.S. Supreme Court granted the state of South Dakota's petition for certiorari in *South Dakota v. Wayfair, Inc.*, No. 17-494 on January 12, 2018 and oral arguments are scheduled for April 17, 2018. The U.S. Supreme Court will issue its decision this year, possibly as early as June, at which time Hawaii and the other states will have an answer on their authority to impose tax on remote sellers. If the U.S. Supreme Court overturns the physical presence standard, this will level the playing field between remote sellers and local brick-and-mortar stores. To the extent the Hawaii legislature wants to take action, it should consider passing an economic nexus law similar to the law South Dakota passed last year. The legislature has introduced two such bills this year – SB 2514 and SB 2508.

Lastly, an immediate effective date is not practical for purposes of compliance. Taxpayers cannot implement the necessary systems changes and compliance procedures quickly enough to be able to comply with HB 1655 upon its enactment. To the extent this Committee feels strongly about advancing HB 1655 as currently drafted, I urge you to consider an effective date that provides taxpayers with adequate time to comply with the law.

For these reasons, Amazon opposes HB 1655 and urges Committee members to consider SB 2514 or SB 2508, which are economic nexus bills that are more inclusive of all sales into Hawaii and provide a clearer standard for compliance. Should you have any questions regarding our position, please feel free to contact me at [bradenc@amazon.com](mailto:bradenc@amazon.com) or 202-442-2900.

Thank you for the opportunity to provide comments.

Sincerely,



Braden Cox